DEPARTMENT OF STATE REVENUE

04-20190149R.ODR

Final Order Denying Refund: 04-20190149R
Retail Sales Tax
For Tax Year 2017

NOTICE: IC § 4-22-7-7 permits the publication of this document in the Indiana Register. The publication of this document provides the general public with information about the Indiana Department of Revenue's official position concerning a specific set of facts and issues. The "Holding" section is provided for the convenience of the reader and is not part of the analysis contained in this document.

HOLDING

Company is not entitled to additional refund because IC § 6-2.5-6-9 explicitly and unequivocally excludes repossessed vehicles from the bad debt calculations.

ISSUE

I. Bad Debt Deduction - Gross Retail Tax.

Authority: IC § 6-2.5-6-9; *SAC Finance Inc. v. Indiana Dep't of Revenue*, 24 N.E.3d 541 (Ind. T.C. 2014); *Caylor-Nickel Clinic, P.C. v. Indiana Dep't of State Revenue*, 569 N.E.2d 765 (Ind. T.C. 1991); *Indiana Dep't of State Revenue v. Horizon Bancorp*, 644 N.E.2d 870 (Ind. 1994); *Perrin v. United States,* 444 U.S. 37 (1979); Black's Law Dictionary (11th ed. 2019).

Taxpayer argues that the Department erred when it disallowed a portion of Taxpayer's refund claim.

STATEMENT OF FACTS

Taxpayer is a finance company for a related "buy-here-pay-here" car dealership. Taxpayer's affiliate sells vehicles to customers on an installment basis and then sells the installment contract to Taxpayer. The installment contract includes the retail price, sales tax, and etc. Taxpayer requested a refund claim of sales tax in which the installment contract was written off as bad debt. The Indiana Department of Revenue ("Department") conducted an investigation of Taxpayer's business records and reduced Taxpayer's refund request. Taxpayer disagreed with that decision and submitted a protest to that effect. An administrative hearing was conducted during which Taxpayer's representative explained the basis for the protest. This Final Order Denying Refund results.

I. Bad Debt Deduction - Gross Retail Tax.

DISCUSSION

Taxpayer requested a refund of on bad debt sales tax included in vehicle installment contracts that defaulted. The Department denied a portion of Taxpayer's refund for the following reasons: duplicated records were removed, insurance fees were removed from total amount financed, and the value of repossessed vehicles were removed from the bad debt calculation. Taxpayer specifically protests that the Department's removal of repossessed vehicles and argues that it should be included in the bad debt calculation. Taxpayer claimed it treated the repossessed vehicles as "partial payments" on the installment contract. These "partial payments" were included in the Taxpayer's calculation of bad debt. This final determination addresses whether the value of repossessed vehicles are considered partial payments on vehicle installment contract and therefore, included in Taxpayer's bad debt calculations.

IC § 6-2.5-6-9 states in part:

> (a) In determining the amount of state gross retail and use taxes which a retail merchant must remit under section 7 of this chapter, the retail merchant shall, subject to subsections (c) and (d), deduct from the retail merchant's gross retail income from retail transactions made during a particular reporting period, an amount equal to the retail merchant's receivables which:
> (1) resulted from retail transactions in which the retail merchant did not collect the state gross retail or use tax from the purchaser;
> (2) resulted from retail transactions on which the retail merchant has previously paid the state gross retail or use tax liability to the department; and

(3) were written off as an uncollectible debt for federal tax purposes under Section 166 of the Internal Revenue Code during the particular reporting period.

(b) If a retail merchant deducts a receivable under subsection (a) and subsequently collects all or part of that receivable, then the retail merchant shall, subject to subsection (d)(6), include the amount collected as part of the retail merchant's gross retail income from retail transactions for the particular reporting period in which the retail merchant makes the collection.

. . . .

(d) The following provisions apply to a deduction for a receivable treated as uncollectible debt under subsection (a):

(1) The deduction does not include interest.

(2) The amount of the deduction shall be determined in the manner provided by Section 166 of the Internal Revenue Code for bad debts but shall be adjusted to exclude:

(A) financing charges or interest;

(B) sales or use taxes charged on the purchase price;

(C) uncollectible amounts on property that remain in the possession of the seller until the full purchase price is paid;

(D) expenses incurred in attempting to collect any debt; and

(E) repossessed property.

(3) The deduction shall be claimed on the return for the period during which the receivable is written off as uncollectible in the claimant's books and records and is eligible to be deducted for federal income tax purposes. For purposes of this subdivision, a claimant who is not required to file federal income tax returns may deduct an uncollectible receivable on a return filed for the period in which the receivable is written off as uncollectible in the claimant's books and records and would be eligible for a bad debt deduction for federal income tax purposes if the claimant were required to file a federal income tax return.

(***Emphasis added***).

Taxpayer argues in its protest that:

> The Department does not apply the literal terms of the Bad Debt Statute, nor does it apply the [Taxpayer's] logical interpretation of the Bad Debt Statute. Instead, the Department interprets "***adjusted to exclude***" repossessed or returned property from the IRC § 166 mathematics as if the Legislature had instead stated that the [Taxpayer] must "***add***" to the [Taxpayer's] federal adjusted basis under IRC § 166.

Thus, Taxpayer is stating that when the Department excludes repossessed vehicles from its bad debt calculations the Department is actually causing Taxpayer to add the repossessed vehicles back to its basis.

Taxpayer also argues that:

> Partial payments and related payments are treated in an economically consistent manner. That is, the portion which is considered an "accretion" of wealth is income, and that portions of which is treated as recovery of basis is not taxable. For example, a payment "with respect to stock" in the form of a divided is taxable income to the shareholder, but does not impact the shareholder's basis in his stock. IRC § 61(a)(7); IRC § 301(c)(1).

Taxpayer explained at the hearing that it has been treating repossessed vehicles as partial payment on the installment contracts. Taxpayer's protest letter states, "First, there is a fundamental distinction between that portion of a receipt which represents (a) a repayment of principal - it is not taxable and reduces the holder's basis, and (b) ordinary income or capital gain - it is taxable income and does not reduce the basis. A payment is one or the other, not both. Second, the foregoing consequences apply regardless of whether the payment is in the form of money or property. Treas. Reg. § 1.1001.-1(a)."

The Department cannot agree with Taxpayer for multiple reasons, however most importantly Taxpayer's calculation directly contradicts IC § 6-2.5-6-9. Indiana's bad debt statute explicitly states that repossessed property should be removed from the calculation of bad debt. To interpret the clear language of the statute otherwise would be to render that language a nullity; this is clearly not the Indiana Legislature's intent.

Taxpayer's interpretation of the statute is contrary to the established cannons of statutory construction as demonstrated by established case law. "[A] statute that is clear and unambiguous on its face needs no further interpretation beyond the plain and ordinary meaning of the words contained therein," and "must be applied and enforced as written." *Indiana Dep't of State Revenue v. Horizon Bancorp*, 644 N.E.2d 870, 872 (Ind. 1994).

"[U]nless otherwise defined, words [in a statute] will be interpreted as taking their ordinary, contemporary, common meaning." *Perrin v. United States,* 444 U.S. 37, 42 (1979). The Department cannot interpret the statute to have meant that repossessed vehicles should be deemed a payment and therefore included in Taxpayer's bad debt calculation. Since "repossession" is not defined in the statute the Department looks to the plain meaning of repossession "The act or an instance of retaking property; **esp., a seller's retaking of goods sold on credit when buyer has failed to pay for them**." Black's Law Dictionary 1556 (11th ed. 2019). (**Emphasis added**). Not only is repossession not defined as a payment, but it is considered a retaking. The Department finds Taxpayer's arguments regarding legislative intent and the need to include repossessed vehicles in its bad debt calculation to be wholly unsubstantiated.

Indiana's case law also supports the Department's interpretation and application of IC § 6-2.5-6-9. First, *SAC Finance Inc. v. Indiana Dep't of Revenue* ("*SAC II*"), interpreted IC § 6-2.5-6-9 to mean that:

> [A] retail merchant (or its assignee) [is required] to deduct the amount written off as uncollectable debt for federal tax purposes under IRC § 166 from its gross retail income. *See* I.C. § 6-2.5-6-9(a)(3). Accordingly, the amount written off under IRC § 166 is incorporated into the Indiana calculation solely as the computational starting point in determining Indiana's bad debt deduction.
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> Indiana Code § 6-2.5-6-9(d) lists the types of revenue that must be excluded from this starting point in calculating the amount of the Indiana bad debt deduction. I.C. § 6-2.5-6-9(d)(1)-(2). **Specifically, Subsection (d) requires a taxpayer to exclude amounts that reduce the original sales tax bases (*i.e.*, the value of repossessed property or property still in the seller's possession)** and that were not part of the original retail sales tax base (*i.e.*, interest, financing charges, sales or use tax, and debt collection expenses) from the difference between gross retail income and the amount of federal bad debt.

24 N.E.3d 541, 546 (Ind. T.C. 2014). (Internal citation omitted) (**Emphasis added**).

SAC II, clearly states that the taxpayer was required to exclude repossessed vehicles from the base calculation. *Id*. The statute clearly states that repossessed vehicles must be excluded from the bad debt calculation. In addition, the Indiana Legislature does not keep a record to elaborate on legislative intent and the courts have decided that the best evidence of legislative intent is the statue itself and that if the Legislature intended to choose specific language the court may not expand or contract the meaning of the statute. *Caylor-Nickel Clinic, P.C. v. Indiana Dep't of State Revenue*, 569 N.E.2d 765, 769 (Ind. T.C. 1991).

In *SAC II*, the Tax Court specifically stated that repossessed vehicles are excluded from taxpayer's I.R.C. § 166 bad debt calculation. 24 N.E. 3d 541, 546. In addition, the Tax Court also stated that, "the portion of each **installment payment** [paid by customer] characterized as market discount income for federal income tax purposes is income that has **actually been paid to SAC** [and not taken by SAC]." *Id*. at 547. Thus, an actual payment is required for market discount calculations and as already stated by the definition, repossession is a retaking, not a payment. Thus, again the Department emphatically cannot agree that Taxpayer is allowed to include repossessed vehicles in its bad debt calculation. And most important IC § 6-2.5-6-9 states, with the utmost clarity, that repossessed property, which includes vehicles, are excluded from Taxpayer's Indiana bad debt collection. Taxpayer's protest is therefore denied.

FINDING

Taxpayer's protest is denied.

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